

# House Study Bill 295

HOUSE FILE \_\_\_\_\_  
BY (PROPOSED COMMITTEE ON WAYS  
AND MEANS BILL BY  
CHAIRPERSON VAN FOSSEN)

Passed House, Date \_\_\_\_\_ Passed Senate, Date \_\_\_\_\_  
Vote: Ayes \_\_\_\_\_ Nays \_\_\_\_\_ Vote: Ayes \_\_\_\_\_ Nays \_\_\_\_\_  
Approved \_\_\_\_\_

## A BILL FOR

1 An Act providing for a tax on earned income of an individual in  
2 lieu of the regular income tax, alternative income tax, and  
3 the tax on lump sum distributions, and including effective and  
4 retroactive applicability date provisions.  
5 BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF IOWA:  
6 TLSB 1510YC 81  
7 mg/cf/24

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1 1 DIVISION I  
1 2 TAX ON EARNED INCOME  
1 3 Section 1. Section 422.5, Code 2005, is amended by adding  
1 4 the following new subsection:  
1 5 NEW SUBSECTION. 11. a. (1) In lieu of the regular and  
1 6 alternative minimum taxes under subsection 1 and the lump sum  
1 7 distribution tax under subsection 7, there is imposed upon  
1 8 every resident and nonresident of the state a tax on the  
1 9 earned income of the taxpayer at the rate of five and thirty=  
1 10 two hundredths percent of the earned income. This subsection  
1 11 does not apply to estates or trusts. The taxpayer must elect  
1 12 to be taxed pursuant to this subsection in the manner provided  
1 13 by rule of the department.  
1 14 (2) The tax imposed under subparagraph (1) upon the earned  
1 15 income of a nonresident shall be computed by multiplying the  
1 16 resulting amount by a fraction of which the nonresident's  
1 17 earned income allocated to Iowa is the numerator and the  
1 18 nonresident's total earned income is the denominator. This  
1 19 subparagraph also applies to individuals who are residents of  
1 20 Iowa for less than the entire tax year.  
1 21 (3) The provisions of subsection 2 relating to the amount  
1 22 of net income upon which no tax is imposed apply to the tax  
1 23 imposed under subsection 1 and do not apply to the tax imposed  
1 24 on earned income under this subsection.  
1 25 b. (1) In calculating the taxpayer's tax liability under  
1 26 this subsection, the taxpayer is not allowed any tax credits,  
1 27 notwithstanding any other provision, unless specified in  
1 28 subparagraph (2) or by rule of the department.  
1 29 (2) The tax credits allowed a taxpayer are all of the  
1 30 following:  
1 31 (a) The nonresident or part-year resident credit.  
1 32 (b) The out-of-state tax credit.  
1 33 (c) The credit for Iowa income tax withheld.  
1 34 (d) The credit for estimated tax and voucher payments.  
1 35 (e) Any other credits allowed against the tax imposed  
2 1 under subsection 1 which the department by rule identifies as  
2 2 appropriate to the fairness of the tax imposed in this  
2 3 subsection.  
2 4 c. A taxpayer's election to be taxed pursuant to this  
2 5 subsection does not affect the taxpayer's ability to designate  
2 6 an amount to be paid pursuant to a checkoff for the Iowa  
2 7 election campaign fund under section 68A.601, a checkoff for  
2 8 the fish and game fund in section 456A.16, or any other  
2 9 checkoff specified in this division.  
2 10 d. If one spouse elects to be taxed under this subsection,  
2 11 then both spouses shall be taxed under this subsection and  
2 12 shall file a joint return.  
2 13 e. For purposes of this subsection, "earned income" means  
2 14 wages, salaries, tips, commissions, and other employee  
2 15 compensation earned from personal services, but only if such  
2 16 compensation is includible in gross income for federal tax

2 17 purposes, without the adjustments specified in section 422.7  
2 18 and the deductions allowed or additions required in section  
2 19 422.9. "Earned income" does not include, but is not limited  
2 20 to, interest and dividends, capital gains or losses, welfare  
2 21 benefits, veterans' benefits, pensions and annuities, alimony,  
2 22 social security benefits, workers' compensation, unemployment  
2 23 compensation, rental income or losses, gambling winnings,  
2 24 self-employment income or loss, income or loss from farming  
2 25 operations, and partnership, limited liability company, or S  
2 26 corporation gains or losses.

#### 2 27 DIVISION II

##### 2 28 COORDINATING AMENDMENTS

2 29 Sec. 2. Section 68A.102, subsection 21, Code 2005, is  
2 30 amended to read as follows:

2 31 21. "State income tax liability" means the state  
2 32 individual income tax imposed under section 422.5, subsections  
2 33 1 and 7, as reduced by the sum of the deductions from the  
2 34 computed tax as provided under section 422.12, or under  
2 35 section 422.5, subsection 11, as applicable.

3 1 Sec. 3. Section 257.21, unnumbered paragraph 2, Code 2005,  
3 2 is amended to read as follows:

3 3 The instructional support income surtax shall be imposed on  
3 4 the state individual income tax for the calendar year during  
3 5 which the school's budget year begins, or for a taxpayer's  
3 6 fiscal year ending during the second half of that calendar  
3 7 year and after the date the board adopts a resolution to  
3 8 participate in the program or the first half of the succeeding  
3 9 calendar year, and shall be imposed on all individuals  
3 10 residing in the school district on the last day of the  
3 11 applicable tax year. As used in this section, "state  
3 12 individual income tax" means the taxes computed under section  
3 13 422.5, subsections 1 and 7, less the credits allowed in  
3 14 sections 422.11A, 422.11B, 422.12, and 422.12B, or under  
3 15 section 422.5, subsection 11, as applicable.

3 16 Sec. 4. Section 422.13, subsection 1, Code 2005, is  
3 17 amended by adding the following new paragraph:

3 18 NEW PARAGRAPH. d. The individual elects to be taxed  
3 19 pursuant to section 422.5, subsection 11.

3 20 Sec. 5. Section 422D.2, Code 2005, is amended to read as  
3 21 follows:

3 22 422D.2 LOCAL INCOME SURTAX.

3 23 A county may impose by ordinance a local income surtax as  
3 24 provided in section 422D.1 at the rate set by the board of  
3 25 supervisors, of up to one percent, on the state individual  
3 26 income tax of each individual residing in the county at the  
3 27 end of the individual's applicable tax year. However, the  
3 28 cumulative total of the percents of income surtax imposed on  
3 29 any taxpayer in the county shall not exceed twenty percent.  
3 30 The reason for imposing the surtax and the amount needed shall  
3 31 be set out in the ordinance. The surtax rate shall be set to  
3 32 raise only the amount needed. For purposes of this section,  
3 33 "state individual income tax" means the tax computed under  
3 34 section 422.5, subsections 1 and 7, less the credits allowed  
3 35 in sections 422.11A, 422.11B, 422.12, and 422.12B, or under  
4 1 section 422.5, subsection 11, as applicable.

#### 4 2 DIVISION III

##### 4 3 EFFECTIVE AND RETROACTIVE APPLICABILITY

4 4 Sec. 6. This Act, being deemed of immediate importance,  
4 5 takes effect upon enactment and applies retroactively to  
4 6 January 1, 2005, for tax years beginning on or after that  
4 7 date.

##### 4 8 EXPLANATION

4 9 This bill imposes a tax at the rate of 5.32 percent on the  
4 10 earned income of an individual. The tax is in lieu of the  
4 11 regular income tax, the alternative minimum tax, and the tax  
4 12 on lump sum distributions. The individual must elect to be  
4 13 taxed on the individual's earned income. The earned income  
4 14 equals the wages, salaries, tips, commissions, and other  
4 15 employee compensation earned from personal services, but only  
4 16 if the compensation is includible in federal gross income.  
4 17 Earned income does not include items such as interest and  
4 18 dividends, pensions and annuities, social security benefits,  
4 19 capital gains, and income from business or investment  
4 20 enterprises.

4 21 The tax on earned income is computed without any of the  
4 22 adjustments listed in Code section 422.7 that are made to  
4 23 federal adjusted gross income; the deductions allowed in Code  
4 24 section 422.9, which includes the standard deduction, itemized  
4 25 deduction, or net operating loss; and the credits otherwise  
4 26 allowed, except for the credit for withholding of income tax,  
4 27 out-of-state tax paid, estimated taxes paid, and others

4 28 designated by the department of revenue that are appropriate  
4 29 to the fairness of the tax on earned income.  
4 30 The bill takes effect upon enactment and applies  
4 31 retroactively to January 1, 2005, for tax years beginning on  
4 32 or after that date.  
4 33 LSB 1510YC 81  
4 34 mg:rj/cf/24